

# Informing the audit risk assessment for Royal Borough of Kingston upon Thames Pension Fund 2020/21



The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect your business or any weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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## Purpose

The purpose of this report is to contribute towards the effective two-way communication between Royal Borough of Kingston upon Thames Pension Fund's external auditors and Royal Borough of Kingston upon Thames Pension Fund's Audit, Governance and Standards Committee, as 'those charged with governance'. The report covers some important areas of the auditor risk assessment where we are required to make inquiries of the Audit, Governance and Standards Committee under auditing standards.

## Background

Under International Standards on Auditing (UK), (ISA(UK)) auditors have specific responsibilities to communicate with the Audit, Governance and Standards Committee. ISA(UK) emphasise the importance of two-way communication between the auditor and the Audit, Governance and Standards Committee and also specify matters that should be communicated.

This two-way communication assists both the auditor and the Audit, Governance and Standards Committee in understanding matters relating to the audit and developing a constructive working relationship. It also enables the auditor to obtain information relevant to the audit from the Audit, Governance and Standards Committee and supports the Audit, Governance and Standards Committee in fulfilling its responsibilities in relation to the financial reporting process.

## Communication

As part of our risk assessment procedures we are required to obtain an understanding of management processes and the Pension Fund's oversight of the following areas:

- General Enquiries of Management
- Fraud,
- Laws and Regulations,
- Related Parties, and
- Accounting Estimates.

## Purpose

This report includes a series of questions on each of these areas and the response we have received from Royal Borough of Kingston upon Thames Pension Fund's management. The Audit, Governance and Standards Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

# General Enquiries of Management

Question	Management response
<p>1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2020/21?</p>	<p>The most significant “event” for the Pension Fund accounts is the impact on asset and liability valuations of market volatility associated with the Covid-19 pandemic, as for all LGPS funds. Illiquid assets may be subject to material valuation uncertainty. However, the majority of the Fund’s assets are currently listed equities and bonds for which prices have remained readily available throughout the year.</p>
<p>2. Have you considered the appropriateness of the accounting policies adopted by Royal Borough of Kingston upon Thames Pension Fund? Have there been any events or transactions that may cause you to change or adopt new accounting policies?</p>	<p>We have considered the classification of illiquid assets (Level 2 and Level 3 assets), given that many property funds were suspended during the year. We are proposing to treat property funds as Level 3 assets going forward.</p>
<p>3. Is there any use of financial instruments, including derivatives?</p>	<p>The Fund itself does not use derivative instruments, loans or other financial instruments directly. The funds in which the Fund invests may use financial instruments within the terms of their investment mandates.</p>
<p>4. Are you aware of any significant transaction outside the normal course of business?</p>	<p>We are not aware of any significant transactions outside the normal course of business during 2020/21.</p>

# General Enquiries of Management

Question	Management response
5. Are you aware of any changes in circumstances that would lead to impairment of non-current assets?	Not relevant to Pension Fund.
6. Are you aware of any guarantee contracts?	Not relevant to Pension Fund.
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	Not relevant to Pension Fund.
8. Other than in house solicitors, can you provide details of those solicitors utilised by Royal Borough of Kingston upon Thames Pension Fund during the year. Please indicate where they are working on open litigation or contingencies from prior years?	There were no major litigation issues during the year, but general advice was sought on some minor administration matters from Bevan Brittan. The Fund uses South London Legal Partnership for day to day legal advice, including review of contracts, in line with the Council's policies and processes. Occasionally where SLLP lack specific technical pensions knowledge, they may refer to external lawyers.

# General Enquiries of Management

Question	Management response
9. Have any of the Royal Borough of Kingston upon Thames Pension Fund's service providers reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements?	None of the Pension Fund's service providers have reported any frauds, non-compliance with laws and regulations or significant uncorrected misstatements.
10. Can you provide details of other advisors consulted during the year and the issue on which they were consulted?	The Pension Fund has received general advice from Hymans Robertson (actuaries), Aon UK Ltd (investment consultants), Pensions for Purpose (responsible investment policy issues), PIRC (performance benchmarking) and JP Morgan (Custodian services).

# Fraud

## Issue

### Matters in relation to fraud

ISA (UK) 240 covers auditors responsibilities relating to fraud in an audit of financial statements.

The primary responsibility to prevent and detect fraud rests with both the Audit, Governance and Standards Committee and management. Management, with the oversight of the Audit, Governance and Standards Committee, needs to ensure a strong emphasis on fraud prevention and deterrence and encourage a culture of honest and ethical behaviour. As part of its oversight, the Audit, Governance and Standards Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As Royal Borough of Kingston upon Thames Pension Fund's external auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error. We are required to maintain professional scepticism throughout the audit, considering the potential for management override of controls.

As part of our audit risk assessment procedures we are required to consider risks of fraud. This includes considering the arrangements management has put in place with regard to fraud risks including:

- assessment that the financial statements could be materially misstated due to fraud,
- process for identifying and responding to risks of fraud, including any identified specific risks,
- communication with the Audit, Governance and Standards Committee regarding its processes for identifying and responding to risks of fraud, and
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Audit, Governance and Standards Committee oversees the above processes. We are also required to make inquiries of both management and the Audit, Governance and Standards Committee as to their knowledge of any actual, suspected or alleged fraud. These areas have been set out in the fraud risk assessment questions below together with responses from Royal Borough of

# Fraud risk assessment

Question	Management response
<p>1. Have Royal Borough of Kingston upon Thames Pension Fund assessed the risk of material misstatement in the financial statements due to fraud?</p> <p>How has the process of identifying and responding to the risk of fraud been undertaken and what are the results of this process?</p> <p>How do the Royal Borough of Kingston upon Thames Pension Fund's risk management processes link to financial reporting?</p>	<p>The majority of the Fund's assets are managed by external third party managers, and therefore reliance is placed on the controls in place at those managers and at the Fund's custodian (for the one segregated mandate). The Fund manages its cash balances internally, according to the frameworks in place to manage fraud risk within the Council. During the year 2020/21, a PF Treasury Management policy was adopted and a separate Pensions Investments team was created, to separate Pension Fund management from day to day management of the Council's cash, to ensure the cash balances of each entity were subject to appropriate scrutiny.</p> <p>The Fund faces the risk of fraudulent pensions claims being made by individuals either impersonating members or claiming that members have died, in order to claim their benefits. These risks are managed by the Pensions Administration team in the normal course of business, through systematic checks of data and documentation.</p> <p>Risks are reported on the Fund's risk register, which is reviewed by the Pensions Panel/Board.</p>
<p>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</p>	<p>No instances of fraud have been noted.</p> <p>Investment related fraud by fund managers or the custodian would be high value fraud, but is deemed unlikely to occur given the regulatory framework under which those entities operate and the systems and controls they are required to have in place when managing client funds.</p> <p>Invoicing fraud by fund managers, custodians, actuaries and consultants is more likely, although again, given these are highly regulated entities, the risk of fraud is deemed lower than in other sectors. Incorrect fee invoicing by fund managers (either due to error, miscalculation or fraud) is the highest risk, given the complexity of fee calculations.</p> <p>Claims/member related fraud is the most likely type of fraud to occur, although generally for smaller amounts.</p>

# Fraud risk assessment

Question	Management response
<p>3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within Royal Borough of Kingston upon Thames Pension Fund as a whole or within specific departments since 1 April 2020?</p> <p>As a management team, how do you communicate risk issues (including fraud) to those charged with governance?</p>	<p>We are not aware of any actual, suspected or alleged fraud, errors or irregularities affecting the Pension Fund during 2020/21.</p> <p>Risk issues are communicated to the Pensions Panel and the Pensions Board (who are responsible for governance of the Fund) via the regular submission of the Fund's risk register to Panel/Board meetings.</p>
<p>4. Have you identified any specific fraud risks?</p> <p>Do you have any concerns there are areas that are at risk of fraud?</p> <p>Are there particular locations within Royal Borough of Kingston upon Thames Pension Fund where fraud is more likely to occur?</p>	<p>We have not identified any specific fraud risks and do not have any specific concerns about areas at risk of fraud. All member benefits paid out are subject to identity checks before payment. All payments are made in accordance with the Council's scheme of delegation, and all invoices paid are subject to the Council's payments control processes and are also checked by the officer commissioning services - given the small number of contracts involved, any unusual invoices or amounts would be queried immediately.</p>
<p>5. What processes do Royal Borough of Kingston upon Thames Pension Fund have in place to identify and respond to risks of fraud?</p>	<p>The Fund's payments processes ensure that all invoices received are checked against existing purchase orders.</p> <p>The Pensions Administration team maintain several levels of checks on lump sum payments and identities of beneficiaries.</p>

# Fraud risk assessment

Question	Management response
<p>6. How do you assess the overall control environment for Royal Borough of Kingston upon Thames Pension Fund, including:</p> <ul style="list-style-type: none"><li>• the existence of internal controls, including segregation of duties; and</li><li>• the process for reviewing the effectiveness the system of internal control?</li></ul> <p>If internal controls are not in place or not effective where are the risk areas and what mitigating actions have been taken?</p> <p>What other controls are in place to help prevent, deter or detect fraud?</p> <p>Are there any areas where there is a potential for override of controls or inappropriate influence over the financial reporting process (for example because of undue pressure to achieve financial targets)?</p>	<p>The Fund's internal controls operate effectively and there have been no incidents of fraud found.</p> <p>Recently action has been taken to introduce a Treasury Management strategy for the fund and segregate the cash management of Council's money from that of the Pension Fund, with different officers managing the cash balances of each entity, to reduce the risk of fraud or error in transferring funds between the Council and the Fund.</p> <p>The Fund has also developed a cashflow model to forecast expected cash movements, which should assist in identifying any unexpected items.</p> <p>Within Pensions Administration, multiple checks and sign offs are required before member benefits are paid, to minimise the risk of fraud (and human error).</p> <p>There are no explicit or implicit financial pressures on officers to achieve financial targets. The Fund sets performance targets for its third party fund managers, but expects those fund managers to have appropriate controls in place to ensure that individuals are not incentivised to achieve those targets fraudulently.</p>
<p>7. Are there any areas where there is potential for misreporting?</p>	<p>The Fund does rely on fund managers, the custodian and its advisers (actuaries and investment consultants) to report financial information accurately, although the risk of inadvertent error is deemed greater than the risk of deliberate fraud.</p>

# Fraud risk assessment

Question	Management response
<p>8. How do Royal Borough of Kingston upon Thames Pension Fund's communicate and encourage ethical behaviours and business processes of it's staff and contractors? How do you encourage staff to report their concerns about fraud? What concerns are staff expected to report about fraud? Have any significant issues been reported?</p>	<p>See Council's response on Fraud reporting and Whistleblowing processes.</p> <p>No fraud issues have been reported relating to the Pension Fund. We are not aware of any whistleblowing reports made, although these could be made to an external regulator without management's knowledge.</p>
<p>9. From a fraud and corruption perspective, what are considered to be high-risk posts?  How are the risks relating to these posts identified, assessed and managed?</p>	<p>High risk posts are considered to be:</p> <p><b>Head of Pensions Investments</b> - signing off performance fees to managers and advisers, could be subject to financial inducement/kickbacks</p> <p><b>Head of Pensions Administration</b> - signing off payments to members, including large lump sum benefits to individuals</p> <p><b>Officers administering cash balances for the Fund</b> - see previous comments regarding segregation of Council cash management from that of Pension Fund, to ensure that no individual can control flows both ways between the two entities. All payments are subject to senior management sign off.</p>
<p>10. Are you aware of any related party relationships or transactions that could give rise to instances of fraud?  How do you mitigate the risks associated with fraud related to related party relationships and transactions?</p>	<p>The Fund's employers are in many cases related parties to each other, and the Fund is required to treat all employers equally. The highest risk is that the Fund gives preferential treatment to the Council, above other employers, or in some way advantages one employer above another, either deliberately or inadvertently. This is mitigated by the requirement for the Fund to be managed by an independent Panel of elected councillors, and its activities scrutinised by a Board comprised of representatives of employers and employees within the Fund. All of the Fund's decisions, policies and significant activities are published online and subject to public scrutiny, unless commercially sensitive. All significant decisions and policies are consulted on with all employers within the Fund. Finally professional advisers, including the actuary, are required to provide advice to the Fund itself rather than any one employer (unless specifically commissioned to provide employers with specific advice) and to be impartial between employers.</p>

# Fraud risk assessment

Question	Management response
<p>11. What arrangements are in place to report fraud issues and risks to the Audit, Governance and Standards Committee?</p> <p>How does the Audit, Governance and Standards Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control?</p> <p>What has been the outcome of these arrangements so far this year?</p>	<p>The Pension Fund reports to the Pension Panel and Pension Board, rather than to the Council's main Audit, Governance and Standards Committee. Any issues of sufficient materiality to affect the Council's financial statements, risk profile or audit, or which have implications for the Council of any sort, will then be escalated to the Audit, Governance and Standards Committee.</p> <p>The Pension Panel and Pension Board regularly review the Risk Register and any regulatory or legal breaches which may have occurred.</p> <p>There have been no instances of fraud or significant control breaches to report to either the Pension Panel/Board or Audit, Governance and Standards Committee</p>
<p>12. Are you aware of any whistle blowing potential or complaints by potential whistle blowers? If so, what has been your response?</p>	<p>We are not aware of any whistleblowing complaints. However, we recognise that we may not be informed of these (if, for example, an individual chooses to whistleblow directly to a regulatory body).</p>
<p>13. Have any reports been made under the Bribery Act?</p>	<p>No reports have been made under the Bribery Act.</p>

# Law and regulations

## Issue

### **Matters in relation to laws and regulations**

ISA (UK) 250 requires us to consider the impact of laws and regulations in an audit of the financial statements.

Management, with the oversight of the Audit, Governance and Standards Committee, is responsible for ensuring that Royal Borough of Kingston upon Thames Pension Fund's operations are conducted in accordance with laws and regulations including those that determine amounts in the financial statements.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error, taking into account the appropriate legal and regulatory framework. As part of our risk assessment procedures we are required to make inquiries of management and the Audit, Governance and Standards Committee as to whether the entity is in compliance with laws and regulations. Where we become aware of information of non-compliance or suspected non-compliance we need to gain an understanding of the non-compliance and the possible effect on the financial statements.

Risk assessment questions have been set out below together with responses from management.

# Impact of laws and regulations

Question	Management response
<p>1. How does management gain assurance that all relevant laws and regulations have been complied with?</p> <p>What arrangements does Royal Borough of Kingston upon Thames Pension Fund have in place to prevent and detect non-compliance with laws and regulations?</p> <p>Are you aware of any changes to the Pension Fund's regulatory environment that may have a significant impact on the Pension Fund's financial statements?</p>	<p>The Fund subscribes to all regulatory updates and consultations via the portals of CIPFA the Pensions Regulator, the LGA, the SAB, GAD, LAPFF, CMA and MHCLG. The Fund's actuaries and investment advisors also provide regular updates on changes to law and regulation, and advise on compliance.</p> <p>LGPS regulation is continually evolving, including retrospective changes to liabilities (eg McCloud remedies) and consultations on planned changes (exit pay). Broader pensions regulation is increasingly being applied to LGPS funds, requiring the Fund to monitor all Pensions Regulator guidance and best practice.</p> <p>Responsible Investment principles also need to be incorporated into management of the Fund's assets.</p> <p>The Fund will continue to monitor the reporting requirements related to evolution in regulation.</p>
<p>2. How is the Audit, Governance and Standards Committee provided with assurance that all relevant laws and regulations have been complied with?</p>	<p>Responsibility for the Fund's governance lies with the Pension Panel and Pension Board, who receive all regular and ad-hoc reports about the activities of the Fund, including the Fund's risk register. The Audit, Governance and Standards Committee would only be notified of significant issues, or issues likely to directly impact the Council, in its role as either Administering Authority or its role as the largest employer within the Fund.</p>
<p>3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2020 with an on-going impact on the 2020/21 financial statements?</p>	<p>We are not aware of any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2020 which would impact the 2020/21 financial statements.</p>
<p>4. Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>We are not aware of any actual or potential litigation or claims that would affect the financial statements.</p>

# Impact of laws and regulations

Question	Management response
5. What arrangements does Royal Borough of Kingston upon Thames Pension Fund's have in place to identify, evaluate and account for litigation or claims?	<p>The Fund does not expect to receive litigation claims in the normal course of business. Any disputes relating to members and benefits are dealt with under the Internal Dispute Resolution Procedure, and are unlikely to lead to litigation.</p> <p>More significant legal challenges facing the LGPS as a whole (eg McCloud and other claims) are monitored closely to determine any potential impacts on the Fund, including the impact of having to increase the value of future liabilities for certain classes of members.</p>
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	<p>There have been no reports of non-compliance from HMRC or other regulatory bodies.</p>

# Related Parties

## Issue

### Matters in relation to Related Parties

Royal Borough of Kingston upon Thames Pension Fund are required to disclose transactions with entities/individuals that would be classed as related parties. These may include:

- entities that directly, or indirectly through one or more intermediaries, control, or are controlled by Royal Borough of Kingston upon Thames Pension Fund's;
- associates;
- joint ventures;
- an entity that has an interest in the authority that gives it significant influence over the Pension Fund;
- key management personnel, and close members of the family of key management personnel, and
- post-employment benefit plans (pension fund) for the benefit of employees of the Pension Fund, or of any entity that is a related party of the Pension Fund.

A disclosure is required if a transaction (or series of transactions) is material on either side, i.e. if a transaction is immaterial from the [type of body]'s perspective but material from a related party viewpoint then the Pension Fund must disclose it.

ISA (UK) 550 requires us to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. We will also carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate.

# Related Parties

Question	Management response
<p>1. Have there been any changes in the related parties including those disclosed in Royal Borough of Kingston upon Thames Pension Fund's 2019/20 financial statements?</p> <p>If so please summarise:</p> <ul style="list-style-type: none"> <li>the nature of the relationship between these related parties and Royal Borough of Kingston upon Thames Pension Fund</li> <li>whether Royal Borough of Kingston upon Thames Pension Fund's has entered into or plans to enter into any transactions with these related parties</li> <li>the type and purpose of these transactions</li> </ul>	<p>There have been no changes to the related parties disclosed in the Fund's 2019/20 financial statements. The Council is a related to party to the Fund, and Council officers (S151) perform duties in relation to both the Council and the Fund. In addition, the Council has a controlling interest in AfC, which is also a member employer within the fund.</p> <p>The decision to create a separate Pensions Investments team within the Council creates greater segregation of duties between the Council and the Fund, with the Pensions Investments team conducting only Pension Fund business.</p>
<p>2. What controls does Royal Borough of Kingston upon Thames Pension Fund's have in place to identify, account for and disclose related party transactions and relationships?</p>	<p>Employers within the Fund are assessed during the triennial valuation and the nature of their relationship with the Council, with the Fund and with each other is scrutinised.</p> <p>Voting members of the Pension Panel are elected councillors and are required to disclose any conflict of interest between their Panel role and their personal connection to the Fund (eg a family member who is a member).</p>
<p>3. What controls are in place to authorise and approve significant transactions and arrangements with related parties?</p>	<p>Individual conflicts of interest are noted at Panel meetings.</p> <p>Transactions with related parties, including employers within the Fund, are approved by the S151 officer.</p> <p>The Fund is required to deal with all employers within the Fund fairly, which is set out in the Funding Strategy Statement and the Pensions Administration Strategy.</p>
<p>4. What controls are in place to authorise and approve significant transactions outside of the normal course of business?</p>	<p>All significant transactions outside the normal course of business, including bulk transfers, require the approval of the S151 officer, in consultation with the Fund's actuary.</p>

# Accounting estimates

## Issue

### Matters in relation to Related Accounting estimates

ISA (UK) 540 (Revised December 2018) requires auditors to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Audit, Governance and Standards Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

We would ask the Audit, Governance and Standards Committee to satisfy itself that the arrangements for accounting estimates are adequate.

# Accounting Estimates - General Enquiries of Management

Question	Management response
<p>1. What are the classes of transactions, events and conditions, that are significant to the financial statements that give rise to the need for, or changes in, accounting estimate and related disclosures?</p>	<p>Most of the Fund's assets are valued on the basis of publicly quoted prices. Property assets have been difficult to value during the Covid19 pandemic and therefore their valuation is subject to material uncertainty, as highlighted by valuers. The Fund's future liabilities are by definition derived from actuarial estimates of eg longevity/mortality, discount rates, pay inflation and member behaviour. They are also subject to uncertainty arising from the implications of government guidance on how to account for retrospective changes to member benefit calculations, including McCloud. Employer exits and entries from/to the Fund, as well as bulk transfers, are initially subject to some degree of estimation of appropriate contribution rates and transfer values, although these are then re-evaluated over time to ensure they remain appropriate and the initial assumptions valid.</p>
<p>2. How does the Pension Fund's risk management process identify and addresses risks relating to accounting estimates?</p>	<p>Asset valuation uncertainty is discussed when necessary with the Fund's investment advisers, custodian and fund managers, to ensure that where uncertainty exists, the most appropriate estimates are used. Liability risks are considered annually in conjunction with the actuary, and are reviewed in detail as part of the triennial valuation process. Employer exits and entries from/to the Fund, as well as bulk transfers, are assessed in line with the Funding Strategy Statement and in practice a long tailed period of negotiations permits subsequent adjustments to valuations to allow appropriate cost recovery/payment.</p>
<p>3. How do management identify the methods, assumptions or source data, and the need for changes in them, in relation to key accounting estimates?</p>	<p>Asset valuations provided by fund managers and reported via the custodian are reviewed for reasonableness - in particular for property assets for which there is no readily observable market price. Liability estimates are reviewed in detail with the actuary on an annual basis, or more frequently if there is a material change (eg McCloud).</p>

# Accounting Estimates - General Enquiries of Management

Question	Management response
4. How do management review the outcomes of previous accounting estimates?	Asset valuations are reviewed quarterly as part of the Pension Panel's review of reported quarterly investment performance. As the Fund is a long term investor, and illiquid assets are a very small part of the Fund's portfolio, any estimates which need to be revised are unlikely to have a material impact on the financial statements. Liability experience variance is assessed formally by the actuaries as part of the triennial valuation process, and reviewed annually to ensure estimates remain reasonable.
5. Were any changes made to the estimation processes in 2020/21 and, if so, what was the reason for these?	No significant changes in estimation processes were made in 2020/21. The actuaries continued to consider the impact of revised government guidance on McCloud implementation and other regulatory changes.

# Accounting Estimates - General Enquiries of Management

Question	Management response
<p>6. How do management identify the need for and apply specialised skills or knowledge related to accounting estimates?</p>	<p>Management seeks guidance from the Fund's actuarial advisers in estimating Fund liabilities, as it is recognised that specialist actuarial knowledge and processes are required to establish an appropriate basis on which to estimate future liabilities.</p>
<p>7. How does the Pension Fund determine what control activities are needed for significant accounting estimates, including the controls at any service providers or management experts?</p>	<p>The Fund's actuaries and advisers are regulated and required to meet standards of professional competence. The Fund's custodian is also regulated and subject to a high degree of regulatory scrutiny. Asset data gathered by the custodian is then checked against information provided by individual fund managers. Fund managers are regulated and required to meet FCA standards in terms of their systems and controls, which provides some comfort that their valuations are reported accurately. For illiquid assets such as property, the Fund will if necessary seek additional information from fund managers on the underlying asset performance.</p>
<p>8. How do management monitor the operation of control activities related to accounting estimates, including the key controls at any service providers or management experts?</p>	<p>In practice the Fund has limited ability to monitor the operation of control activities at its service providers, and must place some reliance on the monitoring performed by the professional firms themselves and their regulators. Advice provided by experts is sense checked against that provided by other market providers, including other actuaries or investment advisers where appropriate.</p>
<p>9. What is the nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates, including:</p> <ul style="list-style-type: none"> <li>- Management's process for making significant accounting estimates</li> <li>- The methods and models used</li> <li>- The resultant accounting estimates included in the financial statements.</li> </ul>	<p>The Fund's annual report and financial statements are presented to the Pension Panel and Pension Board, in draft, for scrutiny and challenge. In addition, the Fund's investment advisors and actuaries are invited to give their opinions on the most appropriate assumptions to be used, where relevant (or in response to external shocks, such as the Covid 19 pandemic). In addition the Government Actuary's Department periodically scrutinises the actuarial calculations and estimates used by the Fund, and benchmarks the Fund to other LGPS funds (Section 13 review).</p>

# Accounting Estimates - General Enquiries of Management

Question	Management response
<p>10. Are management aware of transactions, events, conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgement (other than those in Appendix A)?</p>	<p>Other than those disclosed in Appendix A, the most significant events giving rise to a requirement to disclose and apply significant judgement are likely to be bulk transfers, where final member liability data may not be immediately available. We are not aware of any significant bulk transfer transactions during the FY 2020/21.</p> <p>Judgement may also need to be applied where government consults on retrospective changes to member benefit calculations (eg McCloud, exit pay reforms), where the direction of travel is known but the final rules are not yet defined - management may need to make an estimate based on the most likely of a range of reasonable outcomes, after taking appropriate professional advice.</p>
<p>11. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?</p>	<p>Yes</p>
<p>12. How is the Audit, Governance and Standards Committee provided with assurance that the arrangements for accounting estimates are adequate ?</p>	<p>The arrangements for estimating illiquid asset values and for estimating future pension liabilities are scrutinised by the Pension Panel and Pension Board. Where appropriate, professional advisers provide opinions to management and to the Panel/Board.</p>

## Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Valuation of defined benefit net pension fund liabilities	Fund liabilities are calculated using a number of different methods/models including those used to estimate longevity, discount rates, member behaviour, RPI/CPI, pay inflation, and other key variables.	Actuaries required to disclose the assumptions used to calculate defined benefit net pension liabilities in their professional opinions	Yes - appointed Actuary, Hymans Robertson	Key methodologies are discussed in detail during the triennial valuation process, including sensitivity to changes in assumptions. Actuarial calculations include a margin of prudence. In areas of subjectivity such as interpretation of future changes in regulation (McCloud etc), management need to consider the most appropriate assumptions to use based on their knowledge at that date.	No change in methodology at this stage. Consideration of certain model parameters and inputs eg CPI/RPI, mortality, GMP, IAS 19 transfer calculations, in consultation with actuaries

## Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Level 2 investments (if applicable)	Level 2 investments are primarily pooled investment vehicles, which invest in liquid quoted assets. The value of the investment in the fund is derived from the value of the underlying assets.	Fund managers are required to use observable market prices for assets, where possible, to value their pooled funds. It may be that some less liquid credit instruments do not trade regularly and therefore the fund manager will have derived the valuation based on market comparables, previous trading levels or other methods (discounted cashflows).	Fund manager valuation teams, with input from fund custodians	Most of the pooled vehicles in which the Fund invests, while not themselves liquid traded instruments, do contain primarily liquid traded instruments. It is therefore possible to use the prices of the underlying assets to calculate the value of the investment in the pooled vehicle. Where pooled vehicles contain less liquid instruments (eg certain credit instruments), the fund managers' valuation processes will be used to derive a value for the asset.	No, other than a decision to move Property investments to Level 3 (see below)

## Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Level 3 investments (if applicable)	Property investments - Initial valuations received from fund manager valuations teams. Reviewed for reasonableness.	Fund managers asked to disclose the basis of their valuation process (eg rental yields, occupancy rates, comparable transactions etc) and to disclose any material valuation uncertainty.	Yes - external fund managers appoint professional valuers. Additional input sought from investment advisers where necessary	Assume that valuers will report when their valuations are subject to material valuation uncertainty. Tested against alternative estimates, including other property fund data, previous period data, trends in occupancy/rental yields, property indices etc.	Decision to disclose Property funds assets as Level 3 assets.



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